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**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA**

Rulemaking on the Commission's Own Motion to
Govern Open Access to Bottleneck Services and
Establish A Framework for Network Architecture
Development of Dominant Carrier Networks.

Rulemaking 93-04-003
(Filed April 7, 1993)

Investigation on the Commission's Own Motion into
Open Access and Network Architecture Development
of Dominant Carrier Networks.

Investigation 93-04-002
(Filed April 7, 1993)
(Verizon UNE Phase)

**REPLY COMMENTS OF
THE CALIFORNIA ASSOCIATION
OF COMPETITIVE TELEPHONE COMPANIES**

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I. INTRODUCTION

The California Association of Competitive Telephone Companies (“CALTEL”), on behalf of its members,¹ hereby submits its reply comments in this matter, pursuant to the schedule established by the ALJ.

These reply comments are in response to the opening comments of AT&T California (“AT&T”) and Verizon California (“Verizon”). Both of these carriers oppose the adoption of the CALTEL price caps proposal. CALTEL will address them separately. Neither carrier, however, has offered a single justifiable reason for rejection of the price caps proposal.

Accordingly, CALTEL urges the Commission to adopt the price caps mechanism for adjustment of AT&T’s and Verizon’s wholesale rates.

¹ For purposes of this proceeding, Sage Telecom, while a member of CALTEL, is not a participant in these comments. In addition, CALTEL is supported in these comments by COMPTTEL, which is the leading national industry association representing communications service providers and their supplier partners. Based in Washington, D.C., COMPTTEL advances its member’s business through policy advocacy and through education, networking and trade shows. Like CALTEL, COMPTTEL members are entrepreneurial companies building and deploying next-generation networks to provide competitive voice, data, and video services. COMPTTEL members create economic growth and improve the quality of life of all Americans through technological innovation, new services, affordable prices and customer choice. COMPTTEL members share a common objective: advancing communications through innovation and open networks.

II. DISCUSSION

A. AT&T Is Wrong In Arguing That A Price Caps Mechanism For Wholesale Services Is Unlawful

AT&T's entire response to the CALTEL proposal is an argument that the Commission does not have the legal authority to impose a price caps mechanism on the setting of wholesale rates.² Its theory is quite simplistic – AT&T contends that price caps, which rely on an inflation and a productivity factor, cannot set rates that are TELRIC-compliant. With all due respect, this argument relies on some sort of hypothetical theory of absolute perfection in determining compliance with TELRIC. Federal law does not require such preciseness, nor is it even attainable.

AT&T's argument assumes that one can know precisely what the TELRIC cost of a wholesale element is, and that one can then determine whether a revised rate, calculated using a price caps mechanism, meets that precise cost. Although AT&T properly uses the word “hypothetical” to describe these costs, its argument is instead based on such costs being absolutely precise. This is quite far-fetched and certainly is not required by the law or cases cited by AT&T. Indeed, the Commission has already complied with federal law by setting TELRIC-compliant rates for these services, and now the only question is whether and how to adjust the rates on a going-forward basis.

² AT&T also argues, at p. 1 of its comments, that the CALTEL proposal is procedurally improper. Since AT&T does not pursue this argument, but instead responds to CALTEL on the merits of the price caps proposal, CALTEL will not address the procedural argument. In any event, the procedural appropriateness of considering this issue here has already been resolved by the May 15 order requiring AT&T to respond.

CALTEL's proposal was submitted in order to avoid the costly and time-consuming process of holding never-ending TELRIC cost proceedings. If AT&T's theory of hypothetical perfection were to be carried to its logical extreme, the Commission would have to hold such cost proceedings on an almost daily basis. Certainly the forward-looking costs of providing these wholesale services changes on a regular basis. Using AT&T's theory, the Commission's failure to adjust the rates every single time a cost changes would cause the unchanged rates (set for AT&T in 2004) to be in violation of the TELRIC requirements all of the time. One can easily see how absurd such an approach would be.

AT&T seems to misunderstand the CALTEL proposal. For example, it provides the following incorrect description of CALTEL's proposal:

But CALTEL confuses the issue by interchanging the distinct *actual cost* principles behind price caps and the *hypothetical cost* principles underlying TELRIC pricing. Under price caps, a regulator makes a real world calculation of actual, current costs, and then puts in place a formula for calculating the productivity improvements, with an offset for inflation, that are expected to occur over time.³

This is simply wrong. CALTEL is not proposing that the Commission begin with a "real world calculation of actual, current costs." CALTEL proposes that the Commission begin with the TELRIC-compliant rates previously established for AT&T. Using those rates as a starting point, the price caps plan makes an adjustment to reflect reasonable changes in costs that have occurred over time, as determined by inflation and productivity changes.

Nothing about the price caps plan assumes that these price cap adjustments constitute the actual, direct cost changes in providing the services.

³ AT&T Opening Comments, p. 3.

Inflation and productivity factors are, by their very nature, merely estimates of the changes in costs. Contrary to AT&T's arguments, they are a proxy for a continued analysis of the hypothetical cost incurred by the carriers, as called for by TELRIC requirements.

This is why CALTEL refers to the price caps plan as one that maintains a "nexus" between rates and costs. The word "nexus" implies a "relationship," potentially a close one, and not a direct, precise correlation or calculation. AT&T seems to believe that changes to the rates for wholesale services must only be allowed if they are absolutely equivalent to the TELRIC costs. But once the TELRIC costs were adopted, they have to be adjusted over time or they will not remain TELRIC-compliant. The price caps mechanism proposed by CALTEL is a reasonable method of accomplishing this result.

The Ninth Circuit Court of Appeals, in addressing rates set by this Commission, explained how the process is supposed to work:

"The Telecommunications Act of 1996 provides a single methodology for the setting of rates: TELRIC. '*Federal law requires that any rate for unbundled network elements, adopted by a state commission, comply with TELRIC **when adopted**.*' No provision is made by this law for any rate to be established in a different way." *Verizon California Inc. v. Peevey*, 413 F.3d 1069, 1073 (9th Cir. 2005)(citing *AT&T v. Illinois Bell*, 319 F.3d 402, 411 (7th Cir. 2003)) (emphasis added).

In the present case, the rates for AT&T's wholesale services complied with TELRIC when they were adopted, just as the Ninth Circuit stated they must. The Commission has complied with that requirement, and now it must establish a process for future adjustments to those rates. That is what the price caps mechanism will do.

AT&T's description of the FCC's TELRIC NPRM is simply wrong.⁴ There the FCC asked the following questions:

If the use of productivity factors to adjust rates periodically is feasible, should it be mandatory? Or should states *retain the ability to conduct a full UNE-pricing proceeding at their discretion?*⁵

Note the reference to the “discretion” of the states. They are not required, as AT&T would have it in its comments, to conduct continuous, repetitive, full-blown TELRIC cost proceedings to set the rates for wholesale services (though they may if they want to incur the costs and difficulties of holding such proceedings on a regular basis). Indeed, the process that AT&T itself favors, as established by the Commission in D. 99-11-050, does not even go so far as to require complete cost proceedings on all wholesale rates; it merely permits the nomination of individual UNEs for review.

Moreover, the FCC itself is considering whether to change its rules to require the use of price caps to adjust wholesale rates. That is the very question, cited above, that AT&T seems to want to ignore. There is no federal law that prohibits this Commission from adopting a price caps mechanism now, even in advance of any action by the FCC. Certainly AT&T has not cited any such law in its comments.

⁴ AT&T Opening Comments, p. 4.

⁵ *Notice of Proposed Rulemaking*, Federal Communications Commission, WC Docket No. 03-173, September 15, 2003, ¶ 140 (emphasis added).

B. Verizon Does Not Offer Any Reasonable Arguments In Opposition To The Price Caps Proposal

Verizon's opposition to the CALTEL price caps proposal is similar in many regards to that of AT&T, and suffers from the same flaws. Unfortunately, the Verizon argument says very little beyond conclusory statements that the price caps mechanism is not permitted. In the face of mere conclusory statements and perfunctory citation to case law, there is nothing in Verizon's comments that would justify rejection of the price caps proposal submitted here.

Indeed, one can hardly find any real argument at all in Verizon's comments about the price caps proposal. It contends that the TELRIC rules moved rate-setting away from traditional rate of return regulation, citing *Verizon v. FCC*.⁶ Yet no one has suggested that the Commission use rate of return regulation, so there is no reason why Verizon has even made this assertion. Certainly a price caps adjustment mechanism does not calculate or use any rate of return analysis. This argument makes no sense in the present circumstances.

Verizon cites *Verizon v. Peevey* for the proposition that rates for wholesale services must be TELRIC compliant when adopted.⁷ But CALTEL does not disagree with this point, and it explains above why the Ninth Circuit decision in the *Peevey* case is entirely consistent with the adoption of a price caps mechanism here. This argument by Verizon, to the extent it is even an argument (since it merely consists of the quotation of three sentences from a federal court

⁶ Verizon Opening Comments, pp. 8-9.

⁷ *Id.*, p. 9.

decision), does not support Verizon's objection to the adoption of a price caps mechanism.

The citation to *AT&T Communications v. Illinois Bell*⁸ is a particularly inapt reference. Verizon suggests that this case is directly on point, but the case could not be further from the facts faced in the present situation. In *Illinois Bell*, the Illinois commission had used completely out-of-date, six-year-old costs and rates and then attempted to apply TELRIC inputs to them for purposes of updating the rates. The Seventh Circuit found this to be unacceptable because such out-of-date costs and rates could not themselves be TELRIC-compliant in the first place.

By way of contrast, the Commission here has conducted recent, up-to-date TELRIC rate proceedings for both Verizon and AT&T.⁹ The price caps mechanism would be used to adjust those TELRIC-compliant rates, not to adjust rates set at some long-past date that do not comply with the TELRIC requirements. This is entirely different than the process rejected in *Illinois Bell*, so it is hardly "preempted" by federal law.¹⁰

Verizon's arguments against the price caps mechanism do not, in any way, justify its rejection. Its last statement, that the Commission should "defer ruling on the current UNE rates until such time as a live controversy is before it,"¹¹ is

⁸ *Id.*, pp. 10-11.

⁹ The rates were set in D. 04-09-025 (for AT&T) and D. 06-03-025 (for Verizon).

¹⁰ See also the discussion above of the fact that the FCC itself is considering the adoption of a price caps mechanism. If this were not even allowed, as Verizon suggests, the FCC would hardly be addressing it in an NPRM.

¹¹ Verizon Opening Comments, p. 15.

particularly troubling. CALTEL has offered the price caps proposal in order to obtain some measure of regulatory certainty and to avoid the need for future costly and time-consuming rate proceedings. Verizon merely wants to defer the issue, but the Commission has taken it up here, and the Commission should resolve it here. The appropriate resolution is adoption of the CALTEL price caps proposal.

III. CONCLUSION

Neither AT&T nor Verizon has offered a single good reason why the price caps proposal should not be adopted. In contrast, CALTEL has fully explained why the use of a price caps mechanism would be to the benefit of the Commission, the industry participants and the purchasers of the wholesale services at issue. Use of such a mechanism would reduce or eliminate the need to hold costly, resource-intensive and lengthy cost proceedings, and would provide a measure of price certainty that would benefit all.

For the reasons set forth in CALTEL's opening comments and discussed above, CALTEL urges the Commission to adopt the price caps mechanism for adjustment of AT&T's and Verizon's wholesale rates.

Dated: July 28, 2006

Respectfully submitted,

**California Association of
Competitive Telephone Companies**

A handwritten signature in black ink, appearing to read "J.S. Faber", with a stylized flourish at the end.

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CERTIFICATE OF SERVICE

I certify that I have by mail, and by electronic mail to the parties for which an electronic mail address has been provided, this day served a true copy of the original attached **REPLY COMMENTS OF THE CALIFORNIA ASSOCIATION OF COMPETITIVE TELEPHONE COMPANIES** on all parties of record in this proceeding or their attorneys of record.

Dated July 28, 2006 at Lafayette, California.



Joseph S. Faber

CALIFORNIA PUBLIC UTILITIES COMMISSION

Service Lists

Proceeding: R9304003 - PUC - BOTTLENECK SERVICES

List Name: VERIZON UNE PHASE

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